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Testimony Regarding
H.B. 6763: An Act Concerning Social Innovation
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Human Services
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Senator Moore, Representative Abercrombie, and distinguished members of the Human Services Committee:

I am a Policy Analyst testifying today on behalf of Connecticut Voices for Children, a research-based public education and advocacy organization that works statewide to promote the well-being of Connecticut's children, youth, and families.

"Social impact bonds" (SIB) are a promising method for financing programs that both improves outcomes for children and save taxpayers money. However, we are concerned that these bonds make the State accountable to private investors rather than voters, and could waste precious tax dollars with little benefit to children if they are not well-structured.

H.B. 6763 authorizes State Agencies to enter into contracts with private investors – often called "social impact bonds" – to finance social programs that prevent adverse life outcomes; in theory, these improved life outcomes would save the State money by avoiding future expenditures incurred through efforts to remediate the negative impact of these life outcomes. **As advocates for investments in children, Connecticut Voices is encouraged by the opportunity to leverage private sector financing through social impact bonds to improve outcomes for at-risk children and youth.** Investments in programs that improve the health, education, safety, and general welfare of at-risk children represent an opportunity for fruitful use of SIBs because these investments can help avert negative and expensive experiences like hospitalization, developmental disability, incarceration, or homelessness.

At the same time, Connecticut Voices is concerned that SIBs may make the State accountable to investors who are not residents, voters, or taxpayers, and who have little knowledge about social programs they are financing. Moreover, because SIBs are designed both to save the State money and pay returns to investors, they may create a perverse incentive for the State to reduce needed safety net and treatment expenses for children and families, even in cases where interventions designed to improve outcomes for children and families ultimately prove to be ineffective, in order to save taxpayer dollars and reward investors. In addition, "pay for success" contracts may create perverse incentives for providers to discriminate against parents or families that are less likely to achieve the desired outcome, or to focus on the selected outcomes necessary for payment at the expense of other, more holistic ones. **Specifically, we have the following concerns:**

<u>Accountability to Investors and Taxpayer Waste</u>
No intervention is perfect, and most carry a substantial risk of underperformance. Connecticut should not waste taxpayer dollars paying investors for interventions that do not ultimately save money – **investors should assume the risk that they will not be paid in the case of a failed intervention, not the State.** There are two steps the State can take to ensure that taxpayers do not assume this risk:

- First, Connecticut should structure any SIB it issues so that the State cannot pay out more to investors more than it saves. As written, we are concerned H.B. 6763 does not offer sufficient protection against entering into a money-losing SIB contract. H.B. 6763 requires that contracts be structured so that payments are made only when performance benchmarks are achieved. However, the State could still lose money on such a contract if the contract requires the State to make payments in excess of the true savings realized through the achievement of specified performance benchmarks. (For example, if the State is required to pay $1,000 for each person kept out of the hospital, when in fact preventing the hospitalization saved only $500 per-person.) **We urge the committee to add language mandating that, notwithstanding any other provisions of the bill, no Agency may enter into a contract that could require payments in excess of savings that are *actually achieved* through the financed intervention, with the amount of savings achieved determined by the independent evaluator.**

- Second, Connecticut should evaluate the success of interventions using a randomized control trial (RCT) method, with a live baseline. This means that the State would randomly select who would be eligible to receive the intervention, and the amount of money saved would be determined by comparing the State's expenditures on the intervention population to a randomly selected population that did not receive the intervention. This method is the fairest way of ensuring that measurable outcomes are achieved, and investors are neither over- nor under-paid. Using other methods such as a historical reference group leaves open the possibility that factors external to the intervention – such as changing economic conditions or other unrelated State initiatives – could be responsible for improved outcomes observed in the population targeted by the intervention. In this case, the State could be inadvertently forced to pay investors for savings that were not attributable to the SIB. Currently, H.B. 6763 does not require that interventions be evaluated using an RCT. **We urge the Committee to require that all performance-based contracts be evaluated using an RCT, and that the RCT be used to calculate savings for the purposes of determining payments to investors.**

<u>Perverse Incentives to Reduce Safety Net Services and Treatment Expenses</u>

Because SIBs will likely be designed to save the State money by financing interventions that reduce the demand for expensive safety net and treatment services (e.g., hospitals, foster care placements, special education services, or homeless shelters), these bonds could create a financial incentive for the State and for investors to prevent children and families from receiving care from these safety net and treatment services, even if they are actually necessary. **To avoid this perverse incentive, it is important that interventions be evaluated using a diverse set of metrics that assess holistic well-being, and go beyond just whether the target population for an intervention uses fewer safety-net services.** At minimum, when interventions are targeted at children, these metrics should include measures of whether, after the intervention, children are safe, have access to a loving caregiver, are healthy, have access to excellent educational opportunities, and reside in stable and livable housing. Any intervention that reduces safety net use but that produces worse health, education, or safety outcomes for children and families should be discontinued, regardless of the cost to the State or investors.

<u>Pay for Success and Provider Risk</u>

H.B. 6763 states that SIB contracts should require "payment based on the achievement of... outcomes." **It is also crucial that this "pay-for-success" contracting specifies that *investors* are only paid in the event of successful outcomes, rather than that *providers* of social intervention are only paid in the event of successful outcomes. Providers should be paid for service delivery.** Paying providers only in the event that they achieve certain outcomes creates perverse incentives – to focus on the designated quantifiable outcomes at the expense of holistic child and family well-being, and to cheat or cut corners to achieve otherwise unrealistic goals. Instead of instituting provider "pay for success," providers should be paid for administering a treatment (which is directly in their control) rather than for achieving a designated outcome (which is not). At the end of the contract period, the State can use these outcomes to determine whether the contract should be renewed. It is appropriate that investors be paid only if positive outcomes are actually achieved. However, paying providers for service delivery only ensures that providers never have an incentive to "teach to the test" in order to get paid.

SIBs have the potential to be a valuable source of financing for prevention programs. However, they come with great risk too. We urge the State both to explore a wide range of prevention programs for children that could benefit from social impact financing, and to adopt the recommendations proposed above to ensure that financial interests are never put before those of at-risk children and families.

Thank you for this opportunity to submit testimony regarding H.B. 6763. Please feel free to contact me at kfeder@ctvoices.org or (203) 498-4240 if you have questions or need additional information.